



Memorandum

TO: HONORABLE MAYOR
AND CITY COUNCIL

FROM: Kim Walesh

SUBJECT: SEE BELOW

DATE: February 7, 2013

Approved

Date

2/12/13

COUNCIL DISTRICT: 4

**SUBJECT: APPROVAL OF INCENTIVES FOR THE DEVELOPMENT OF
SAMSUNG'S R&D CENTER IN SAN JOSE**

RECOMMENDATION

Adopt a resolution authoring the City Manager to execute the following agreements:

- (a) An Incentive Agreement between the City of San José and Samsung Semiconductor, Inc. outlining the City and State incentives to be provided to Samsung in coordination with the development of the proposed Research and Development (R&D) Center in North San José.
- (b) A Capital Equipment and Assistance Agreement with Samsung Semiconductor, Inc., in which the City will provide an amount not to exceed \$500,000 for the acquisition of production and assembly equipment to be installed at Samsung Semiconductor's new R&D facility in San José.
- (c) Utility Users Tax Reimbursement Agreement with Samsung Semiconductor, Inc., that will provide funding in an amount equal to 50% of the City's 5% of net new utility user taxes received from Samsung Semiconductor for 10 consecutive years in an amount not to exceed \$500,000.

OUTCOME

Approval of these Agreements will help Samsung Semiconductor redevelop and expand their 300,000 square foot headquarters facility at 3655 North First Street into a new 680,000 square foot facility. Samsung will invest in capital acquisition for their new facility and support at least 2,000 jobs.

BACKGROUND

Samsung Semiconductor, Inc. has been headquartered in San José, California since 1986 and is a wholly owned U.S. subsidiary of Samsung Electronics Co., Ltd., the second largest semiconductor manufacturer in the world and the industry's volume and technology leader in DRAM, NAND Flash, and SRAM memory and TFT-LCD panels. Samsung Semiconductor's five business units—Memory, TFT-LCD, Storage, Foundry and System LSI—provide advanced solutions for the mobile, desktop computing, consumer electronics and industrial markets communication systems.

As Samsung prepared to expand its R&D headquarter facility in North America, it explored alternative locations for the new investment, including Austin, where it has a very significant presence.

On June 19, 2012, Council directed staff to initiate collaboration with the County of Santa Clara and the State of California regarding incentive programs that could be made available by the three parties if necessary to companies that commit to generating jobs and investing in R&D and manufacturing facilities in San José. R&D tax credits, Employee Training Panel funds and Enterprise Zone benefits are State programs that San José has previously used effectively for economic development purposes.

As a result of the collaboration between the City, State, and County, a Memorandum of Understanding between the parties was announced by Governor Jerry Brown and signed by the Governor, Mayor Chuck Reed, Santa Clara County Board of Supervisors President George Shirakawa and Samsung President Jong Joong Kim of Samsung on August 16, 2012.

The Memorandum of Understanding outlined economic development incentives to be offered by the City of San José and the State of California. City of San José incentives include expedited permitting, a utility user tax rebate, traffic impact fee reduction, \$500,000 capital reimbursement for eligible equipment purchased, and eligibility at the R&D/office rate for the construction tax. Other incentives are to be provided to Samsung through State of California programs and include participation in the Enterprise Zone, R&D tax credits, and an allocation of training dollars from Employment Training Panel (ETP) funds. A further description of the incentives is provided below.

ANALYSIS

Samsung currently has more than 370 employees at their 300,000 square foot R&D facility, spread over three buildings. Samsung's intent is to build a state-of-the-art Research and Development Center in San José to drive innovation in Samsung's semiconductor business globally. The R&D center would consist of approximately 680,000 square feet of facilities that would support at least 2,000 jobs. The proposed development includes two 10-story towers, a restaurant and meeting space. Samsung's architects have created a sophisticated design that

embodies the aspirations of the new North San José Plan - higher density, green, pedestrian friendly, transit-oriented, architecturally significant.

Prior to choosing a San José location, Samsung was strongly considering a location outside of California. The support from the City and State, as demonstrated by financial commitment, was viewed as critical to maintaining the company's operations in San José and securing the significant additional investment.

As a charter city, under its municipal powers the City may provide financial assistance to entities that will be of public benefit to the City. With regard to the incentives to Samsung Semiconductor, the investment in a new facility will be a public benefit to the San José by preserving and expanding the number of jobs and revenues to the City.

A. City Incentive Agreement

1. Traffic Impact Fee Reduction

In January 2012, Council approved the Traffic Impact Fee (TIF) Reduction in order to accelerate development in North San José as the economy started to recover. The incentive allows a reduction in the TIF if the project is over 100,000 square feet, building permits are obtained by December 31, 2014, and the building receives a Certificate of Occupancy by December 31, 2016. The program allows one million square feet of development. Through the program the current TIF is reduced from \$13.54 per square foot to \$5 per square foot. The value of the TIF program to Samsung is roughly \$3.9 million. Council approval of the TIF incentive program also delegated authority to the City Manager to negotiate and sign related documents for implementation of the TIF incentive. Council authorization in January 2012 identified the potential loss of revenue to the City as a result of the TIF incentive.

2. Expedited Permitting

The proposed incentive program provides that the City meet a 120 day time-frame for issuing the site development permit for the project. Samsung filed for their Site Development Permit on January 3, 2013. Samsung's development team has been working collaboratively with the City's Development Services team and the project is proceeding well. Staff anticipates that the site development permit for the project will be heard at Director's Hearing on March 20, 2013, well within the specified time frame.

3. Construction Tax Reduction

The Samsung project is a Research and Development use and qualifies for the (1%) industrial Construction Tax Rate as set forth in Municipal Code Chapter 4.46.

4. Use Tax Program

When companies purchase from vendors or suppliers outside the State of California, the City may not receive the full one percent of associated use tax. The Use Tax Program is a partnership between Samsung and the City through which Samsung assists the City in recouping associated use tax. The Program guidelines will allow Samsung to recover approximately twenty percent of the net new use tax revenues that could accrue to the City through the Use Tax Program. Any remittance paid to Samsung would only occur after receipt of net new use tax dollars to the City. To facilitate any potential distribution to Samsung, an appropriation would be included in the budget at the appropriate time.

In a traditional sales tax transaction, the City receives 1% of the sales tax. By way of example, if Samsung bought a \$5 million dollar piece of equipment from a San José business, the amount of sales tax revenue the City would receive would be \$50,000. When Samsung purchases the same good from out of State, most of the time, the use tax the City would receive would only be \$21,500, as a result of tax money flowing into the Santa Clara County wide pool. Under the Use Tax Program, Samsung would designate and accrue any use tax from out of state equipment purchases having first functional use in San José. As a result, the City would thus receive the full \$50,000. Under ordinance 28640, Use Tax Incentive Program, the City would reimburse \$10,000 to Samsung leaving the City with \$40,000.

5. Enterprise Zone Benefit

The City will assist Samsung in taking advantage of the State's Enterprise Zone tax credits. Currently, the hiring tax credit is worth \$37,440 per eligible employee over a five year time frame which is subject to modifications by the state legislature. The Enterprise Zone also provides, state corporate income tax credit on all computers, copiers, faxes, and R&D/manufacturing/assembly equipment equivalent to the amount of sales and use tax paid.

6. Capital Investment Incentive Program

The Capital Investment Incentive Program (CIIP) is a statewide program that allows counties and cities to share property tax dollars to incent economic development. The CIIP program cannot be implemented at the current Samsung site at this time due to existing fiscal constraints imposed by property tax related obligations. If the tax related obligations at the current site are fulfilled in the next 10 years, the State of California, the County of Santa Clara, and the City of San José agree to enter into good faith negotiations to enact and execute necessary actions to provide CIIP or other comparable benefits to Samsung.

B. Utility Users Tax Reimbursement Agreement

The City charges a five percent (5%) utility tax on gas and electricity. Samsung will receive a Utility Users Tax rebate that allows a 50% reduction in the new Utility User Tax collected by the City over a ten-year period. The City's financial assistance shall be payable from net new Utility Users Taxes in the City's General Fund revenues and will be available if Samsung completes

construction of a building program of not less than \$200 million. The City shall reimburse Samsung an amount equal to fifty percent (50%) of the net new Utility Users Tax over the current base on an annual basis. The amount of the rebate will not exceed \$500,000 over the ten-year period. Construction of the building is intended to be complete in 2015. The Utility Users Tax rebate would initiate after construction completion. The necessary budget actions to recognize the additional revenue and appropriate the associated tax rebate will be brought forward as part of the City's budget at the appropriate time.

C. Capital Equipment and Assistance Reimbursement Agreement

The City will assist in the acquisition of capital equipment exclusively for the industrial, manufacturing and research and development uses on the premises. The City shall reimburse Samsung up to \$500,000 for eligible equipment. Upon receipt by the City of a Request for Reimbursement together with confirmation that the equipment has been installed, the City shall reimburse Samsung up to the \$500,000 amount. If for whatever reason, Samsung ceases operations at the premises in the first year of operation, Samsung must reimburse the City the full amount of assistance provided to the company. If Samsung remains in occupancy on or beyond the seventh anniversary of occupying the facility, Samsung shall not be required to reimburse the City for any portion of the Capital Equipment incentive. The Capital Equipment and Assistance Agreement specifies certain repayment amounts if Samsung ceases to operate in the facility prior to the seventh year of occupancy. A city-wide Economic Development/Incentive Fund appropriation in the 2012-2013 Adopted Budget is available as a funding source for this purpose. No new funds are requested.

EVALUATION AND FOLLOW-UP

City staff will monitor Samsung Semiconductor's expansion and employment contributions. City staff will provide progress updates to the Community and Economic Development Committee.

PUBLIC OUTREACH/INTEREST

- ☒ **Criterion 1:** Requires Council action on the use of public funds equal to \$1 million or greater. **(Required: Website Posting)**
- ☐ **Criterion 2:** Adoption of a new or revised policy that may have implications for public health, safety, quality of life, or financial/economic vitality of the City. **(Required: E-mail and Website Posting)**
- ☐ **Criterion 3:** Consideration of proposed changes to service delivery, programs, staffing that may have impacts to community services and have been identified by staff, Council or a Community group that requires special outreach. **(Required: E-mail, Website Posting, Community Meetings, Notice in appropriate newspapers)**

This item meets Criterion 1, copy of the City Council memo will be posted to the City's website for the February 26, 2013 meeting.

COORDINATION

This memo has been coordinated with the City Attorney's Office and the City Manager's Budget Office.

FISCAL/POLICY ALIGNMENT

The project aligns with the City's Economic Development Strategy #3 "Preserve and Strengthen Manufacturing-Related Activity and Jobs."

Staff prepared a Cost Benefit analysis for the proposed Samsung development. The initial findings show that the proposed development has a positive net fiscal benefit to the City and Successor Agency to the Redevelopment Agency of San José.

Benefits

- Economic impact related to Construction: Over \$475 million
- Estimated net annual property revenue: \$2 million to the Successor Agency to the Redevelopment Agency of San José
- Annual economic impact of the new facility: \$385 million
- Net present value fiscal impact to City's General Fund: Approximately \$168,000
- 1,600 new jobs in research and development, and an estimated 900 jobs related to construction activity
- A new campus with higher density that reflects the vision of the North San José plan
- Housing impact: None, no units will be constructed or demolished
- Neighborhood impact: All neighborhood impacts were included in the North San José Plan and in General Plan 2040

COST IMPLICATIONS

The costs (\$500,000) associated with the Capital Reimbursement Program will be funded by the city-wide Economic Development/Incentive Fund appropriation. It is anticipated that the Traffic Impact Fee incentive will result in a loss of revenue (\$3.9 million). The necessary budget actions to recognize the revenues and expenditures for the proposed Utility Users Tax and the Use Tax Program will be brought forward as part of the City's budget at the appropriate time.

HONORABLE MAYOR AND CITY COUNCIL

February 7, 2012

Subject: Capital Equipment and Assistance Agreement with Samsung Semiconductor, Inc.

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BUDGET REFERENCE

Fund #	Appn #	Appn. Name	RC #	Total Appn	Amt. for Contract	Adopted Budget (Page)	Last Budget Action (Date, Ord. No.)
001	3535	Economic Development/ Incentive Fund	TBD	\$750,00	\$500,000	IX-7	6/19/12 Ord. No. 29102

CEQA

Public Project Number PP10-066(a), Equipment Acquisition.

/s/

KIM WALES

Director of Economic Development
Chief Strategist

For questions please contact Nanci Klein, Deputy Director of the Office of Economic Development at (408) 535-8184.